

**EXECUTIVE SECRETARIAT**  
ROUTING SLIP

*Memo Chono*

TO: *PA*

		ACTION	INFO	DATE	INITIAL
1	DCI		X		
2	DDCI		X		
3	EXDIR				
4	D/ICS				
5	DDI	X			
6	DDA				
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8	DDS&T				
9	Chm/NIC				
10	GC				
11	IG				
12	Compt				
13	D/OLL				
14	D/PAO				
15	D/PERS				
16	VC/NIC				
17	D/OGI/DI		X		
18	D/Exec Staff		X		
19	A/ES		X		
20	D/ALA		X		
21	Amb Dailey		X		
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SUSPENSE		Date			

Remarks

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*PA* Executive Secretary  
22 OCT 86  
Date

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The Director of Central Intelligence

Washington, D. C. 20505

Executive Registry

86-4887

22 October 1986

MEMORANDUM FOR: DDI

FROM: DCI

SUBJECT: Third World Attitudes  
Toward Capitalism

I agree with your evaluation of the Pat Kennon paper on Third World Attitudes Toward Capitalism. I would distribute it to a wide audience of senior officials who are involved in US economic policy. I would have someone like [ ] or 25X1 [ ] take a look at it for suggestions as to how some detailed and operational thrust of value might be put into it. Also, I would have Pete Dailey take a look at it with that in mind.

  
William J. Casey

25X1

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Central Intelligence Agency  
Office of the Deputy Director for Intelligence

DDI #04550X/86/1  
2 October 1986

NOTE TO: Director of Central Intelligence  
Deputy Director of Central Intelligence

SUBJECT: Third World Attitudes Toward Capitalism

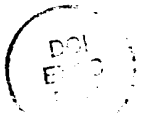
My first reaction to this paper by [ ] 25X1  
[ ] was that it did not provide enough 25X1  
detail on how we might take advantage of changes  
in Third World attitudes toward capitalism.  
But I think Pat has developed a useful framework  
for thinking about actions that we might take.  
I would be inclined to distribute this paper  
to a fairly wide audience of senior officials  
who are involved in US economic policy. I am  
uncertain whether it would be more useful in  
its current form or as a finished document.

*Dick*  
Richard J. Kerr

Deputy Director for Intelligence

Attachment:

DDI #04550X/86, dtd 30 Sep 1986



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DDI- 04550X/86

30 SEP 1986

MEMORANDUM FOR: Director of Central Intelligence  
Deputy Director of Central Intelligence

VIA: Deputy Director for Intelligence [redacted] 25X1  
Associate Deputy Director for Intelligence [redacted] 25X1

FROM: [redacted] 25X1  
Director of Global Issues

SUBJECT: Third World Attitudes Toward Capitalism

1. Action: Request that you review the attached think piece on changing Third World attitudes toward capitalism and determine whether you would like to send it to anyone.

2. Background: The report was prepared by [redacted] in response to your interest in the issue of how the West can best compete with the Soviets in the Third World. The report is more of a think piece along the lines of the one [redacted] did on structural change about a year ago. We will be integrating many of his ideas into the Third World opportunities study which we expect to have ready in early December. [redacted] 25X1

Attachment:  
As stated

All portions Secret

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29 SEP 1986

NEW ATTITUDES TOWARD CAPITALISM: A WINDOW OF OPPORTUNITY  
IN THE THIRD WORLD AND A STRATEGY FOR TAKING ADVANTAGE OF IT

The world intellectual climate is more favorable today for capitalism, free enterprise, and the market system than at any time during the past fifty years. The new popularity of capitalism, however, will not automatically result in gains for the United States nor in losses for the Communist Bloc. Unless policymakers have a clear understanding of what the new climate is--and, equally important, what is not--why it arose and why it will eventually weaken, a unique opportunity may be lost. This loss is all the more probable because taking advantage of the opportunity to its fullest could entail serious short-term costs for some sectors of the US economy. Opposition from vested interests, both here and abroad, will be strong. Moreover, despite a growing rejection of Marxist economics that has now become almost total, the Communist system will continue to provide powerful political and military attractions for the less stable countries of the Third World.

This paper, frankly speculative, is based on a study of Third World attitudes as revealed in: (1) USIA and other polls; (2) publications assessing business conditions in foreign countries for international investors; and (3) a wide range of Third World newspapers and magazines. The information so obtained is sketchy, sometimes inconsistent, and flavored by the biases of the original writers. Nevertheless, we believe that this body of information, taken as a whole, indicates a sharp and continuing change in popular and elite attitudes towards economic

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organization.

### A Sea Change in Attitudes

In the middle of the last century, Karl Marx elaborated a "historical law" whereby socialism would "inevitably" replace capitalism. Until recently, both advocates and opponents of economic statism suspected that Marx might have been at least half right. Although rigid Soviet-style collectivism was already beginning to lose its luster, democratic socialism, the welfare state, and Third-World variants of all of these seemed to be the wave of the future. Even in Third World countries where the market system was firmly entrenched, leaders found it expedient to give lipservice to socialism. Public opinion polls indicated that both elites and masses found capitalism and free enterprise distasteful if not actually evil. Nationalization and evermore extensive government control were the preferred answers to all economic problems.

The picture is very different today. State-owned firms are being "privatized" from Brazil to Bangladesh, from Mexico to Malaysia, from Turkey to Tanzania. The few polls we have indicate that privatization is generally popular and that the private sector is being seen with increasing respect. Public leaders who once pretended that their countries were more socialist than was actually the case now pretend that their countries are more capitalist. India, for many the premier nation of the Third World, and China, the world's largest Communist state, are both seen as increasingly enthusiastic converts to the market

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system. Even the Organization of African unity has agreed that "the positive role of the private sector is to be encouraged." In Western Europe Socialists are pushing deregulation, and in Eastern Europe Communist leaders are speaking up for "market solutions." "Structural reform", a code-word for drastic cutback in the economic influence of the state, has replaced statism as the panacea for economic and social ills.

### Characteristics of the Change

It would be a mistake, however, to assume that the new attitude towards capitalism--especially in the Third World--is a blanket endorsement of the US economic system or of US economic policies. Based on limited polling data and a reading of the Third World press, it appears that Japan is more favored as an economic model than the United States. (Apparently, no one favors the USSR as an economic model, including those elements of the Third World press that defend it in all other realms.) It may be that the experience of Japan--which was an LDC within the memory of many living Third World policymakers--seems more relevant because of the level from which Japan started and the speed with which it progressed. South Korea is also cited as a model, though less frequently.

Perhaps because of the Japanese example, government is not considered an enemy of capitalism. Although much Third World opinion supports privatization and is scornful of the corruption and inefficiency associated with state enterprises, there is a general feeling that the state should "direct" the economy and

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"work with" the private sector. Indeed, government-private sector cooperation is often cited as the key to the economic success of Japan, South Korea, Taiwan, and Singapore as well as the earlier and now faded "miracles" of Brazil and Mexico.

A variety of sources indicate that Third World public opinion increasingly supports foreign investment. (In this respect, the people may be ahead of the leadership in many countries.) At the same time, many apparently feel that foreign investment should operate within a framework set by the state or negotiated between states. Moreover, most believe that certain sectors of the economy should be set aside for domestic investors. Although some potential foreign investors are favored over others--Japan, the United States, and France being among the favorites--the idea of "balancing" investors appears to be more popular with governments than with the public as a whole. Public opinion often seems to favor a "partnership" with a single more powerful country.

In summary, a worldwide shift in popular attitudes in favor of capitalism and against statism is under way. In the Third World, the shift is characterized by:

- o An admiration for Japan and the other East Asian success stories.
- o A belief that most parastatals are inefficient and corrupt and drags on the economy.

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- o A concern that some "strategic" industries should remain under government control and probably under government ownership.
- o A belief that private enterprise is most successful when it works with and is directed in a general way by a wise government (such as that of Japan).
- o A belief that foreign investment works best when it is in the context of an agreement between governments.

The characteristics of the shift differ from country to country and from group to group and are still evolving.

#### Reasons for the Change

Why did this shift in attitudes happen? Not because the world suddenly studied the problem, marshalled the facts, and became intellectually convinced of capitalism's superiority. All of the arguments for capitalism and against statism had been known--and rejected--for decades. Nor was it from an objective comparison of the records of capitalist and socialist economies. Such comparisons have long been commonplace, but whereas once public opinion explained away the successes of the United States and made excuses for the failures of the Soviet Union, now public opinion ignores the continuing problems of such aggressively capitalist nations as the United Kingdom and Chile and focusses on US and East Asian successes. At present, the new

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attitudes are based on faith and fad. If the new attitudes are to become permanent, the faith must be justified before the fad dies.

### The Influence of the "Future"

Just as the Nineteenth Century was the age of laissez-faire capitalism, so the Twent~~y~~h<sup>th</sup> Century is an age of social revolution. The first twentyfive years of this century--which saw profound revolutions not only in Russia but also in China, Mexico, Persia, and Turkey as well as attempted revolutions from India to Morocco, from Brazil to Berlin to Budapest--set the tone for the years to follow. Not that revolutions were always successful--usually they were not--but they defined the questions, the hopes, the fears, and the philosophies of several generations. From student cafes to government ministries talk centered around such questions as: Revolution or reform? Stalin or Trotsky? Communism or Fascism? Has the working class been coopted? Is the New Deal too late? Will Marx be proven right in the Third World? Can capitalism survive?

These questions now seem as "old Hat," as far from present-day reality as the theological disputes of the Middle Ages. They are increasingly the domain of aging professors, tired hacks from major parties, and crazed ideologues from minor parties. These questions, and their answers, are not so much right or wrong as uninteresting, out of style. What does Lenin have to do with microchips? Or Revolution with the rise of Japan? The feeling is that the Twentyfirst Century is almost here--and whatever it

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turns out to be, it will not be the age of social revolution!

Like many other intellectual trends, the new popularity of capitalism seems to have begun in Paris. Possibly it started with Jean Jacques Servan-Schreiber, whose book The American Challenge, published in 1967, told Frenchmen that the forces that were changing the world had nothing to do with revolution and everything to do with capitalist economics. This was followed in 1970 by Jean-Francois Revel's Without Marx or Jesus and the works of the French "New Philosophers". The hidden message of all these works was that statism, Marxism, and revolution were "the wave of the past." And no Third World intellectual wants to concern himself with what the Paris intelligencia considers passe.

#### The Influence of Hard Times

It is significant that the turn toward capitalism came just as much of the world was suffering recession. Part of this is easily explicable. Countries seeking foreign loans have every incentive to take some steps toward limiting the government role and to promise still more. When dealing with bankers and the IMF, it pays to talk like a born-again capitalist. The leaders of the major Third World debtor nations know this and act accordingly. What is less obviously explicable is the public approbation that generally meets these moves. In country after country, organized labor makes only token protests as real wages plummet and even the leftist press speaks in terms of "austerity" and "responsibility." Cuts in food and transportation subsidies,

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which often create riots even in times of prosperity, seem to have become less sensitive. The big story in many LDCs is "the riot that didn't happen."

All of this bespeaks a certain sobriety that hard times bring to ordinary people. It appears that, when times are good, those who do not share the general prosperity feel cheated and look to the state to redress the balance and those who prosper feel uneasy and assuage their guilt by upholding leftist causes. Populists appeal to both groups. When times are bad, however, there is a growing realization that hard measures must be taken. The workers, already suffering, want to assure themselves that their suffering will have a payoff. The not-so-poor, feeling that they may be the next victims of the economic decline, want something done before it is too late. Populist rhetoric does not ring true and soon dies down, while leaders who promise work and sacrifice--for a purpose, of course--are applauded as realistic.\*

In most Third World countries there is a basic stratum of free enterprise "penny capitalism" that is submerged in times of prosperity and comes to the forefront in times of hardship. This stratum constitutes the family background of almost all Third World urbanites, except the highest political and commercial elites. Small merchants, market women, shoeshine boys, cab

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\*Despite conventional wisdom to the contrary, the historical record shows both popular agitation and the appeal of extreme left-wing movements tend to die down during times of economic hardship. Communism's greatest popularity in the developed countries, for example, came during the booming 1920s, not during the depressed 1930s.

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drivers, free-lance artisans, self-taught carpenters and plumbers, these are the people who remain when factories are closing and bureaucrats are losing their jobs. These people, from their own experience, have an intuitive understanding of the connection between hard work and prosperity, between saving and wealth, between spending and saving. When times are good, they are quite willing to take whatever "magical" benefits the free-spending state has to give. When times are bad, however, they are realistic enough to know why.

#### A First Step

The first step in taking advantage of the new attitude towards capitalism should be an appeal to the penny capitalist sector. These people are attuned to local needs and are used to making a buck under local conditions. They are hard working, ingenious, and have a thoroughgoing respect for the profit motive. They are also undereducated and sometimes dishonest by developed world standards. Though forced by circumstances to think small, they are capable of thinking big--many of the Third World's most dynamic businessmen had their origins in the penny capitalist sector.

Reaching these people with the proper proposals will be difficult. US businessmen have no dealings with them. They belong to no local Chamber of Commerce. They are not on the list of contacts of the Commercial Attache. Perhaps it would be easier to attract them than to seek them out. If the proper combination of financing and technology to fit a local need were known to be

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available, these people would probably come forth with their own proposals. These proposals should be carefully studied--the penny capitalist sector is the source of con-men as well as entrepreneurs--and only those accepted that use local knowledge to take the concept farther than originally envisioned by its US sponsors. The local entrepreneur must bring his own ideas to the project if it is to be truly successful.

Neither the US government nor US businessmen are used to working in this environment, and the natural tendency to rely on old patterns of thought must be avoided. This is not a Peace Corps-type exercise to better people's lives by introducing new seeds or hoes with longer handles, nor is it a typical business operation to set up a local plant to take advantage of a local market. It is not intended to garner good will for the United States or profits for US businesses. It is intended to strengthen indigenous capitalism in the Third World by combining US technology and financing with local knowledge and ambition, thereby raising local living standards and helping to counter extremist ideologies.

#### The End of the Era of Materials

A second, more ambitious, step is also possible. The world economy is changing rapidly and in ways that are often unpredictable, and in these circumstances the capitalist nations--or at least some of them--are in a better position to ride the

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wave of the future than are the rigid, unresponsive command economies of the Communist Bloc. This change, which promises to be as profound as the Industrial Revolution, will wreak havoc not only among Communist and Third World nations but also in many capitalist countries. Changes of this magnitude cannot be tamed just by mouthing the right slogans or passing the right laws. In the Twentyfirst Century, capitalism will be a necessary but not sufficient condition for economic wellbeing; a country must also have intelligence, adaptability, and luck. Some Third World countries may make the grade; some developed nations may not.

Larson, Ross, and Williams, in their epochal article "Beyond the Era of Materials" (Scientific American; June 1986), establish that the industrial countries "are now leaving the Era of Materials, which spanned the two centuries following the advent of the Industrial Revolution, and are moving into a new era in which the level of materials will no longer be an important indicator of economic progress." They give four reasons for this: (1) substitution of common for rare materials; (2) increased efficiency of materials use; (3) saturation of markets; and (4) the low materials content of evolving new markets. They believe that market saturation is the most important of these reasons and argue persuasively that replacement and maintenance of established networks of housing, factories, roads, etc--even on a massive scale as in Europe and Japan after World War II--cannot provide the kind of long-term economic stimulus that was provided by their initial creation.

The implications of the end of the era of materials are

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profound and far-reaching:

- o The real value of most commodities will continue to decline, with predictable results for those countries and regions that depend on commodity exports. This affects everything from Russian oil to Zambian copper to Kansas wheat.
- o Countries without strong resource bases, such as Japan and Taiwan, are no longer at a disadvantage to other nations.
- o The remaining unsaturated markets for the broad range of material goods are all in the Third World or the Communist Bloc--and effective demand from these countries is reduced because of the low earnings of their commodity exports.
- o In a saturated market, protectionism and export subsidies can at best slow the decline of a materials-based industry. This is equally true of Japanese shipyards, European farms, and American auto plants.
- o As the cost of materials in any given product declines relative to that of labor, the tendency for basic industry to relocate in low-cost countries will intensify.

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- o Those developed nations that continue to emphasize basic industry will stagnate or decline. This will even be true of countries such as the United Kingdom and West Germany--whether ruled by socialists or free-enterprise conservatives--to the extent that they continue to rely upon steel, oil, automobiles, and basic chemicals.

### Taking The Second Step

Some benefits for the West will accrue from the first step. Still others will come automatically from the current shift in attitudes, but these benefits may not be profound or long lasting.\* Indeed, they may not survive the next development of French philosophy or the next round of "easy" prosperity. If permanent benefits are to be derived, the Western powers must actively take advantage of this limited window of opportunity. Luckily, the West--and especially the United States--is well equipped to take such advantage.

In our opinion, the best results with regard to any particular Third World country can be obtained by following a four-point strategy. First, work with the trend, not against it. Second, create new elites because the old elites, with few exceptions, are too enmeshed in the old way of doing things to be

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\* Although the shift to a post-industrial world that favors the market system and capitalist organization is probably unstoppable, the recent popularity of capitalism depends in large part on changeable intellectual currents that have only a loose connection with real-world economic life.

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part of a new capitalist revolution. Third, tame the many and varied vested interests against the change. Finally, coopt <sup>and</sup> masses by bringing them a level of benefits clearly not obtainable under the old system. This strategy will depend heavily on the cooperation of the private sector in the developed countries and on the large multinational corporations in particular. Putting such a strategy into effect will not be easy, but it does offer great prospects for success.

#### Working With the Trend

The most important trend to take advantage of is the shift of basic industry from the developed countries to selected countries of the Third World. Despite developed nation policies--based on job concern, strategic concern, or simple fear of "deindustrialization"--intended to stop this shift, the transfer of smokestack industry is accelerating. Manufacturing in the United States, for example, which provided 30 percent of national income in 1960, provides only 21 percent today. Many Western firms have little choice; they can shift a part of their production to the Third World, they can go bankrupt, or they can hide behind ever more expensive tariffs and quotas. As there is little or no possibility of successfully bucking this trend, Western governments should attempt to guide and use the trend to facilitate a wide range of political and economic objectives.

The development of a new capitalist basic industry sector in selected LDCs would be profitable for both sides. What the United States should offer Mexico and Brazil (or France should offer Algeria, or Germany Turkey, or Japan India) is the

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opportunity to become major industrial powers, supplying the bulk of basic industrial goods not only to the saturated markets of the developed world but also to still unsaturated regional markets in the Third World. What the United States (or France, or Germany, or Japan) should demand in return are: (1) a degree of control through private-sector joint ventures and other relationships sufficient to insure acceptable levels of quality and security of supply; (2) an understanding, such as the United States has with Panama concerning the Canal, that in times of war or other emergency a new set of rules would come into play; (3) political stability and compatability; and (4) a commitment on the part of the host country to promote a similar shift of some of its own low-tech industry (i.e. textiles, etc.) to its less-advanced neighbors so that these neighbors can earn foreign currency to buy basic industrial goods from the more advanced LDCs.

Obviously, the creation of the new capitalist sector will require decades to accomplish. Within the context of agreed-upon goals, progress would have to be piecemeal. Infrastructure would have to be developed, workers trained, technology adapted in the developing country. In the developed country, workers would have to be retrained and factories retooled for higher-technology applications. In most cases, the pace of the shift could probably be left to the economic decisions of the private firms involved and their Third World partners. As subsidies and other protective measures are removed, each country would produce at its most efficient (and profitable) level of technology. Most

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very high tech production would remain in the developed countries for the foreseeable future.

Although the effort would be primarily directed and financed by the private sector, Third World governments would have to be brought on board for several reasons. First and foremost, public opinion in the Third World believes that government should have a say in economic matters. Second, governments must provide the political stability and compatability needed to gain the trust of the developed nations and the private firms involved. Finally, an antagonistic government--even if weak--could effectively prevent the shift from taking place. In dealing with Third World governments, the developed country government should concern itself only with what is most important--honesty, efficiency, predictability, stability--and not worry about historical and philosophical differences.

#### Creating New Elites

Typically, in the Third World the public sector is used to huge losses and the private sector is equally used to huge--if insecure--profits. The one has no real deadlines for "building the nation," and the other requires a 100 percent gain in twelve months or it won't risk its money. Both sectors are more skilled at working around problems than solving them, more skilled at taking advantage of government policies than of economic opportunities, more inclined to rely on contacts and influence than on good ideas and hard work. If a viable new capitalist sector is to be created, a new elite is needed. Without such a new elite, the new sector will remain nothing more than a

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developed-country "colony" in an otherwise underdeveloped country.

We believe that the required new elite, given the proper incentives, will be self-selecting. One source of the new elite will be the penny capitalist sector. Another source may be the lower and middle management--down to shop foremen--of the relocated industry. It is only necessary to promote rapidly and reward lavishly those employees who consistently solve problems and come up with effective ideas. Small promotions and piddling rewards will not do the job; the right man should have the opportunity to rise from the shopfloor to the board room in ten years. Any slower pace will not serve to create an elite. It is equally important not to make token promotions, even token promotions to the board room, of people whose only attributes are English language ability, company loyalty, or family connections.

Another source of recruits for the new elite may be the relocated industry's local suppliers. Here again, results should be rewarded. Local suppliers who consistently supply high-quality goods and services within fixed deadlines should not only get the relocated company's business, they should get loans and technical advice that will allow them to expand. The owners of these firms should have at least as good an opportunity to get rich as the influence peddlers and political fixers of the old elite.

For the new elite to function as an elite, it must have a certain critical mass. The group must be large enough so that members can support each other, maintain their status against

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other elites, and recruit new members. Although too much visibility can be counterproductive, even dangerous in some countries, the new elite must have enough visibility to influence on non-elite thinking. The entrepreneur should become as acceptable to a role-model as the politician or the narcotics kingpin. Public opinion, as we have shown, is increasingly accepting capitalism as the wave of the future; it should be more than ready to accept the new elite as the bearers of that future.

#### Taming Vested Interests

The creation of new elites is a difficult, but necessary part of the strategy, because vested interests on every side will be trying to limit the new capitalist sector. Leaving aside vested interests in developed nations--which are many and powerful--there are at least four groups of vested interests in the developing nations: the political authorities; the management and workers of the state sector; the nationalists, often including the armed forces; and the private businessmen and their employees. Given the change in attitudes towards capitalism, all of these groups except the nationalists will probably give a degree of lipservice to privatization and economic freedom; all, however, will also fear rapid moves in that direction.

It is important to allay the fears of the political authorities. Most Third World governments are extremely weak, and their primary political task--from the point of view of the leadership--is not to diffuse power to the people but to amass enough power in the state to avoid anarchy. Thus, the political leadership, even if it does not have a statist economic ideology,

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will fear the creation of a strong private sector that could become a rival center of political power. To allay these fears, it may be advisable initially to establish the relocated industries in enclaves or free-trade zones well away from the capital or other politically sensitive areas of the country. In any event, it should be made clear that the new capitalist sector has no intention of mounting a political challenge to the government.

The parastatals fall into three groups: those companies that the state is highly unlikely to give up, i.e. communications, perhaps oil and mining; those companies that the private sector does not want, i.e. antiquated steel mills and the like; and those companies that are profitable under government management but have no strategic importance, i.e. hotel chains, perhaps airlines. Going with the trend, the state should be encouraged to maintain its control over the first category of parastatals--it is going to do this anyway--while making them more efficient and divesting some ancillary operations. If properly handled, the divestment could give profitable opportunities to part of the management and workforce of the parastatal--and thereby create supporters of privatization. The government should also be encouraged to close the clearly failed parastatals, with the new capitalist sector offering to create new industry in the same geographic area. The profitable non-strategic parastatals could become a part of the new capitalist sector, perhaps through debt-equity swaps, with the original management and workforce remaining in place for a period of time.

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The nationalists, whose interest in the issue is patriotic or ideological rather than material, cannot be completely tamed. In time, if the new capitalist sector is successful in bringing prosperity to the nation and creating a domestic elite, the nationalism issue may take care of itself. In the interval, the new capitalist sector can lower its profile by publicly stating that it has no interest in taking over strategic industries--however defined--nor in influencing the course of domestic politics.

The domestic private sector, which may be nearly as corrupt and inefficient as the state sector, is in many respects the natural enemy of the new capitalist sector. These high-markup, low-volume firms often exist only by virtue of protective measures (if producing for the domestic market) or by direct or indirect subsidies (if producing for export). They could not survive in the regulatory climate necessary for the new capitalist sector. Often the loudest proponents of laissez-faire capitalism in the abstract, these domestic big businessmen will use all their influence to keep it from happening in practice. Some few may have the attitudes and talent to join or even to lead the new capitalist sector, but others will continue to block economic progress until they go under. In most Third World countries, however, they are an isolated group and unlikely to find allies among other elements of the domestic elite.

#### Coopting the Masses

Many years will have to pass before relocated basic industry and its suppliers will be in a position to supply jobs for the



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masses of people in the Third World. Indeed, an early effect of industrial relocation may be the worsening of unemployment in the immediate area, because of the internal migration of job-seekers. In order to maintain and enlarge the consensus for the opening of capitalism, visible benefits must accrue both to workers in the new capitalist sector and to those left outside.

Within the new capitalist sector, the support of the workforce can generally be obtained through good wages, decent working conditions, and exceptional opportunity for advancement for talented workers. In some countries unions can be helpful in this regard; in others the union mentality would be so adverse to the new initiatives that a union-free workplace would be worth fighting for. There are a number of mistakes to be avoided:

- o Do not try to gain favor by featherbedding or using excessively labor-intensive methods. More points can be gained by creating a profitable, state-of-the-art industry than by sopping up unskilled labor.
- o Be very selective in the use of profit-sharing or employee-ownership programs. In many Third World countries, such plans are regarded as "dodges" to avoid paying "just" wages.
- o Do not insist on cultural norms that have nothing to do with getting the job done. Mexican workers, for example, have rebelled against exercise groups and

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common worker-manager mess halls that Japanese firms have tried to institute.

In general, local customs should be followed--but not to the point where they interfere with productivity.

The bulk of the population outside the new capitalist sector can still benefit. The increase in local national prosperity created by the industrial shift will increase jobs in construction, retailing, and personal services. Government infrastructure projects--better education, roads, airports, power grid expansions--that the new capitalist sector will demand and pay for through its taxes, will benefit the population as a whole. Perhaps most important in coopting the masses will be a new sense of pride that their country is now "one of the big boys," exporting high-quality products around the world.

#### The Rest of the Third World

It is only to be expected that the industrial shift will intensify divisions that already exist within the Third World. The initial industrial shift will benefit those countries on the Pacific rim and in parts of Latin America, South Asia, and North Africa where the process is already under way. Most of the other Third World countries, lacking suitable workforce or infrastructure, will initially have little to offer the developed world. As the process progresses, however, commodity producers should profit from increased raw-material demand as the new capitalist sector takes hold in the NICs. Over the longer run,

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some of these countries will be able to take over the low-tech assembly and other manufacturing now being done in the more advanced LDCs.

Unfortunately, some LDCs probably will not benefit from the industrial shift in any way. Some will prove inhospitable to the new capitalist sector because of nationalism, ideology, or simple fear of losing control. In others, problems of infrastructure and workforce will inhibit the transfer of even low-tech assembly-type industry from the more advanced LDCs. Both of these groups may find themselves falling out of the world economy. They may be forced into a kind of primitive autarky, ameliorated only by tourism, some handicrafts, and limited exports of raw materials. Even in their autarky, however, these countries can benefit from the transfer of appropriate technology to their penny capitalist sectors from the West. Such technology will not relink them with the world economy but will aid their domestic economies and improve the lives of their people.

#### The Continuing Soviet Challenge

The new attitude towards capitalism--reflecting as it does a major structural change that is under way in the world economy--will provide political opportunities for the capitalist countries. It will not, however, undermine one of the greatest attractions of the Communist system--the promise of political control. The Soviets have long since ceased to compete with the West in terms of economic progress or quality of life. What they and their East German intelligence advisors and Cuban presidential guards offer the Third World is a defense against

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anarchy. The closer anarchy lies below the national surface, the more appeal the Communist system will have. In this respect, Ethiopia--a state of rebellion pretending to be a nation--provides greater opportunities for the Soviets than, say, Venezuela or Thailand.

To the extent that establishment of the new economic sector demands--or appears to demand--increased political liberalization relative to the norm of the country involved, we can expect that its establishment will be resisted. Some countries may attempt to combine capitalist economics with Communist politics in an effort to achieve prosperity with control. We see elements of this approach from Hungary and China to Mozambique. Others may seek non-Communist authoritation solutions similar to those of the East Asian and Latin American NICs. Still others may deliberately choose control over prosperity. We should not underestimate the appeal of the Communist police-state to political and military elites who fear being swept away by a tide of tribalism, regionalism, class conflict, and intra-elite rivalries.

### Conclusion

Recent world-wide intellectual currents favoring capitalism, though shallow, reflect important structural changes that are taking place in the world economy. While these more favorable attitudes will fade as intellectual fashions change, we expect the structural changes to continue and intensify. At present, the developed capitalist countries are in a position to use the

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window provided by new attitudes to direct the change in a way that will: (1) protect the strategic interests of the developed countries; (2) create a firm base for prosperity and capitalist organization in selected Third World countries, thereby firmly linking these countries to the capitalist world; (3) spread lesser but still important benefits to other, less-advanced LDCs; and (4) counter, to some extent at least, the attraction Communist police-state methods hold for fearful Third World governments. The first step would be to strengthen local capitalism by providing suitable technology and financing to entrepreneurs from the penny capitalist sector.

The second step consists of a four-point strategy of going with the trend, creating new elites, taming vested interests, and coopting the masses. We believe this strategy is well based, considering the following facts:

- o A shift of basic industry to the Third World is taking place. Those countries, developed and developing alike, that adapt to the shift will prosper; those that fight it will suffer. Just as New England's present high tech prosperity is in part the result of the migration of its textile industry to the South and overseas, so too will the developed countries prosper in the post-industrial world to the extent that they cede basic industry to the Third World. MITI has already suggested that it should be official Japanese policy to cede steel, aluminum, and textiles to other countries.

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- o Previous manufacturing ventures in the Third World have been largely aimed at the internal market. To the extent that these firms were foreign-owned and directed, they did little to foster capitalist growth and were often resented as examples of "neocolonialism." To the extent that the firms were locally owned and directed, they often produced inferior goods at high prices and gave "import substitution" the bad reputation that it has among economists in the developed and (increasingly) the developing worlds. This type of industrial transfer has few advocates today.
- o The present industrial shift--while it retains elements of the earlier pattern--aims at creating export-oriented basic industry producing world-class goods through state-of-the-art techniques. Unlike the situation in the past, there is no place in the new capitalist sector for the transfer of antiquated capital equipment that is no longer suitable for modern industry in the developed countries.
- o Although close connections exist with developed-country firms, the new capitalist sector is characterized by the creation of new local elites. This process is most advanced in the East Asian NICs. Japanese capital and technology, for example, were necessary for the

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establishment of South Korea's steel industry, but ownership, management, and industrial strategy quickly passed into Korean hands. While the speed and completeness of this process will differ from country to country, it must eventually take place if the new capitalist sector is to become a viable force.

- o Given that in the Twentyfirst Century most US steel, aluminum, basic chemicals, and automobiles will almost certainly be coming from the Third World, it is to the US advantage to have a say in the location of relocated industry and the structure and ownership of the new industrial firms. Japan's increasing interest in the Mexican steel industry--obviously aimed at the US market--is an example of the possible dangers of unguided structural change.

Governments in both developed and developing nations have important roles to play in the industrial shift. The developed country government must be willing to facilitate the shift of much of its industrial base as part of a long-term plan that includes non-discriminatory acceptance of the developing country's production. The developing country must be willing to create the physical and social infrastructure and the legal environment in which the new capitalist sector can prosper. Initially, neither country will be able to fulfill its role completely because of domestic pressures; in time, however, the

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**advantages of the shift should be apparent to both sides and additional steps less difficult.**

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